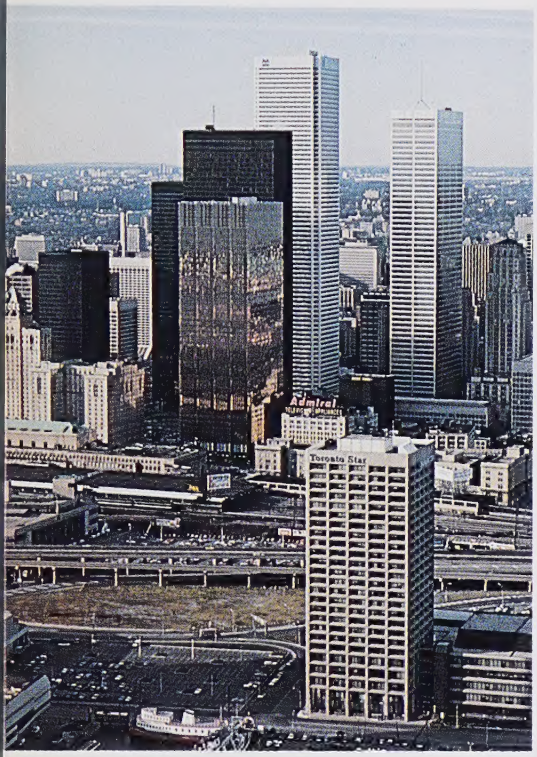
Torstar Corporation Annual Report 1977

Torstar Corporation is a diversified communications company with primary interests in newspaper and book publishing. Toronto Star Newspapers Limited publishes Canada's largest newspaper. Harlequin Enterprises Limited is the world's largest publisher of romantic fiction. Other Torstar activities include magazine and community newspaper publishing, commercial printing, electronic data services and film production.

TORSTAR



Corporate offices and The Toronto Star are located at One Yonge Street, adjacent to the shopping and financial core of Toronto.

The cover
The description of the Corporation found on this year's cover is cast into a flat lead plate, and then photographed. This plate represents Torstar's printing and publishing operations, the base from which the Corporation is expanding in the communications field.

THE CORPORATE ORGANIZATION

Management Company
Torstar Corporation

Newspaper Publishing
Toronto Star Newspapers Limited
Metrospan Community Newspapers Limited
Southstar Publishers Limited (50%)

Books and Learning Materials
Harlequin Enterprises Limited (53%)

Printing, Magazines and Film Production
Commercial Printing — Toronto Star Rotogravure Division
— Newsweb Enterprise Limited
Comac Communications Limited (95%)
INFOMART (50%)
Nielsen-Ferns Inc. (80%)

Broadcasting Investment
Western Broadcasting Company Limited (33%)

Head Office
One Yonge Street
Toronto, Ontario
M5E 1P9
(416) 367-4595

Transfer Agent and Registrar
National Trust Company, Limited

Listed
Classes B & C Shares
Toronto and Montreal Stock Exchanges

BOARD OF DIRECTORS

Beland H. Honderich,
Chairman

William A. Dimma,
President

Burnett M. Thall,
Vice-President

William J. Campbell

Ruth Atkinson Hindmarsh

Harry A. Hindmarsh

Alex J. MacIntosh

Walter L. Gordon

Lionel C. Mohr,
Vice-President

Catherine Atkinson Crang

Richard A. N. Bonnycastle

Martin Goodman

The advertising community was given a preview of the new Sunday Star at a special presentation on September 7. Guests were greeted by (from left) Editor and Assistant to the President Martin Goodman, Chairman and Publisher Beland Honderich and President William Dimma.
First edition of The Sunday Star rolled off the presses on the morning of October 16.

Report to Shareholders

The past year has been a difficult and challenging one for your Corporation. Substantial progress was made in many areas, particularly the book publishing operations of Harlequin Enterprises Limited, acquired in October, 1975. These gains were largely offset by a sharply reduced contribution from newspaper operations, resulting in an essentially flat year for consolidated earnings.

Consolidated operating revenue was $220,851,000, an increase of 14% over 1976 revenues of $193,001,000. Net income before extraordinary item was $11,919,000 or $1.47 per share, which represents only a marginal increase over 1976 results of $11,690,000 or $1.45 per share.

Extraordinary tax reductions were realized in both years, increasing net income per share to $1.51 in 1977 and $1.58 in 1976.

Newspaper Operations

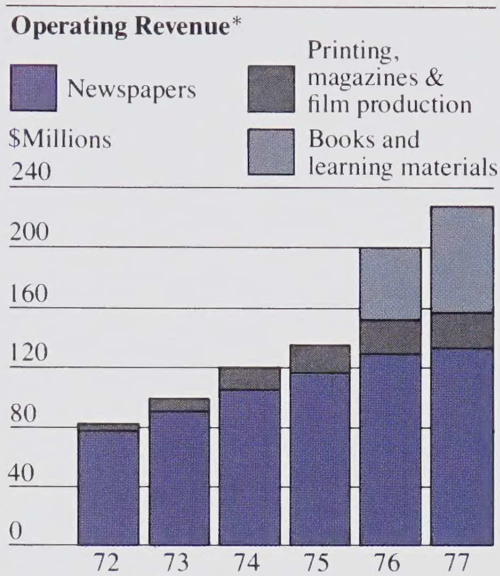
The slowdown in the Canadian economy in 1977, accompanied by lower consumer spending and high unemployment, resulted in a 7% drop in advertising linage in The Toronto Star. This had a proportionately higher effect on newspaper operating profits which were down by 38% from 1976. Significant recovery depends on improvement in current economic conditions. In the meantime, costs are being controlled tightly with the objective of off-setting the start-up costs for Sunday and avoiding a further decline in newspaper operating profit.

The Sunday Star

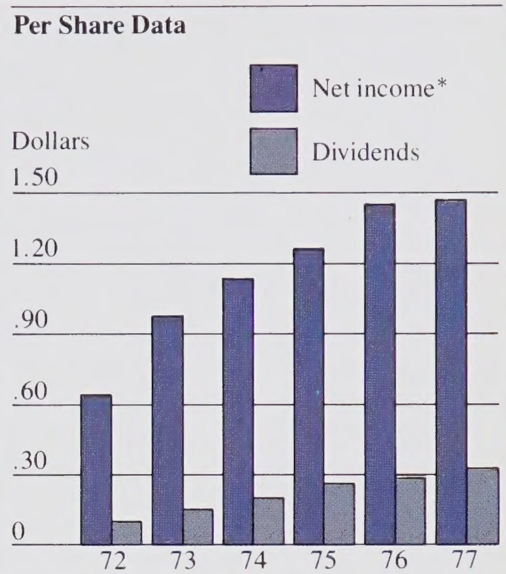
The Directors of the Corporation decided at a Board meeting on July 20, 1977 to proceed with seven-day publishing of The Toronto Star. The first issues of The Sunday Star, and its companion color magazine, The City, were published October 16.

The impact on 1977 results of the Sunday start-up was a charge against operating revenues of $600,000. All introductory costs of The Sunday Star and The City magazine are being written off as incurred and the Corporation is budgeting for a significant charge against 1978 operating revenues.

In content, The Sunday Star, delivered in the morning, is meeting reader needs for the latest news and sports coverage and also is providing unique columns and features geared to more leisurely Sunday reading habits. Both the Sunday newspaper and the inclusion of an entirely new magazine format provide additional opportunities for present and new Star advertisers.



*includes intercompany printing revenue



*excluding extraordinary items

The Saturday Star

The Saturday Star, with circulation of more than 780,000, is growing and is also delivered in the morning to provide increased advertiser and reader convenience. Star Week, a weekly guide to TV viewing, dining and entertainment, is a major feature of the Saturday paper and has been expanded and improved. The Saturday Travel section is the largest and most comprehensive compilation of travel news and advertising in the market. Significant changes have also been made in editorial and advertising approaches in the "New in Homes" section.

The Canadian Magazine, a national weekend supplement which is a regular feature of the Saturday Star, has expanded the flexibility it offers both national and local advertisers by providing target market editions. With the issue of January 7, 1978, The Canadian will further expand its Toronto market appeal by including Toronto editorial coverage on special Cityspan pages which will be available only in copies distributed with The Toronto Star.

The Star's circulation continues to rise in absolute terms with Monday to Friday circulation averaging 492,254 on a 12-month basis ending September 30 and Saturday circulation averaging 780,677. Comparative 1976 figures were 488,942 Monday to Friday and 768,532 on Saturday.

During 1977 The Star renewed its collective agreements with its craft unions. These agreements called for wage increases of approximately 8% retroactive to January 1, 1977 and approximately 6% effective January 1, 1978. Negotiations will be held in fiscal 1978 with The Toronto Newspaper Guild representing the majority of Star employees. The Guild contract expires December 31, 1977.

Data on The Toronto Star newspaper

Advertising linage (000's of lines)	1972	1973	1974	1975	1976	**1977**
Display	31,561	33,194	33,571	34,173	36,572	**34,058**
Classified	18,033	18,692	21,979	21,643	20,598	**18,992**
Total	49,594	51,886	55,550	55,816	57,170	**53,050**
Circulation (12-month average)						
Monday to Friday	507,249(1)	509,679	502,802	484,426	488,942	**492,254(2)**
Saturday	701,959(1)	746,376	739,899	749,847	768,532	**780,677(2)**

(1) The 11-month period (November 1971 to September 1972) was used for 1972 because of a substantial increase in circulation beginning on November 1, 1971.

(2) As filed with the Audit Bureau of Circulations, subject to audit.

Harlequin Enterprises Limited publishes more than 100 million books per year in several languages. Handy new display carousel (inset) places books in an attractive and eye-catching setting.
Good typography and attractive design make Harlequin books easy to read any time, even during commuting trips by bus or subway (far right).

Metrospan Community Newspapers Limited

Nine local community newspapers in fast-growing Metro Toronto locations continued to show steady progress. Circulation of these papers exceeded 234,000 copies weekly. In September, market penetration was further expanded in the Scarborough, Etobicoke and North York areas of Metropolitan Toronto by addition of a new publication, The Consumer. Introduction of The Consumer, which brings Metrospan penetration to 75% in the three boroughs, has been satisfactory. Metrospan marketing efforts are being expanded to take advantage of reader and advertiser response. The nine weeklies and The Consumer reflect Torstar's ongoing determination to provide both readers and advertisers with a selection of media which best suits their needs.

Harlequin Enterprises Limited

Book publishing was an exceptionally strong factor in the Corporation's 1977 performance. Harlequin Enterprises Limited increased sales by 48% and more than doubled its operating profit in the 12-month period to September 30. Harlequin, of which Torstar now owns about 53% of equity, contributed 36 cents to Torstar's $1.47 earnings per share. This calculation reflects the effect of additional shares issued to acquire Harlequin as well as goodwill and carrying costs of the investment. In 1976, the first year of control, it is estimated that the investment reduced per share earnings by 6 cents. Thus, the counter-cyclical nature of Harlequin's book business has been dramatically demonstrated during a year in which some of Torstar's advertising-related operations have experienced a downswing.

Harlequin's success results from aggressive management programs designed to increase penetration in existing markets, to introduce the Harlequin concept to new markets and to diversify into related fields.

Book sales world-wide are presently running at an annual rate in excess of 100 million copies in the English, German and Dutch languages. Translations are also published under license in several other languages.

The United States remains one of the fastest growing markets and accounts for more than 80% of Harlequin's North American book sales on both a unit and dollar basis. Sales in the United States were up substantially over the previous year on both a unit and dollar basis, and Canadian sales also continued to grow.

The Harlequin Reader Service experienced substantial growth in 1977. The service, which provides subscribers with a selection of titles by mail on a monthly basis, has developed strong reader loyalties.

Expansion into new markets has also been a strong point in 1977. A West German joint venture, Cora Verlag KG, was finalized with the Axel Springer Group this past year to publish and distribute not only translated Harlequin romances, but to introduce other lines as well. In Holland, six books per year are published in the Bouquet Reeks series and two books under the Jasmijn label have been added. In the United Kingdom, Harlequin's British company, Mills & Boon, experienced much improved results.

In July, Harlequin purchased Ideals Publishing Corp. of Milwaukee. Ideals is engaged in publishing and distribution of magazines, books, prints and greeting cards.

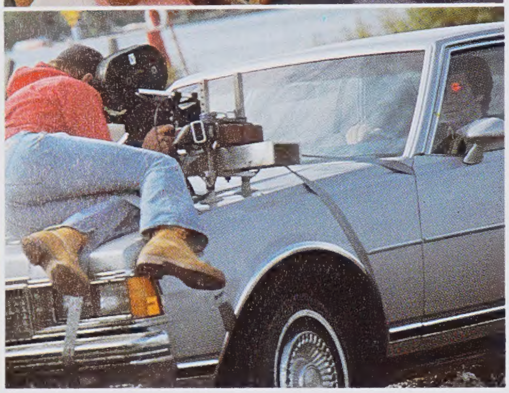
Leopard In The Snow, a full-length feature film co-produced in 1977, will be released in early 1978. It is a faithful representation of a Harlequin novel of the same name and is designed to test the proposition that well established markets for Harlequin's books can provide related opportunities for Harlequin-based motion pictures.

Comac Communications Limited

Controlled circulation magazines continue to be the fastest growing segment of the Canadian consumer magazine market. Comac, which publishes three such magazines — Homemaker's, its French language counterpart Madame Au Foyer, and Quest — recorded a 25% increase in net advertising revenue in 1977.

Homemaker's/Madame Au Foyer continued in 1977 to carry more pages of advertising to women than any other magazine in Canada. Quest's increase in advertising revenue amounted to 50% and came as a result of a dramatic rise in several major advertising categories including financial, automotive and leisure goods.

Growing reader and advertiser acceptance prompted an increase in publishing frequency in 1977, with Homemaker's/Madame Au Foyer going from eight to nine issues and Quest adding a seventh issue.



Nielsen-Ferns, Inc. broadened the range of its productions during the past year, including the filming in Toronto of four episodes of the British spy-action series The New Avengers.

Printing

The commercial printing division experienced lower revenues in 1977, but an improved contribution, largely from rotogravure operations. An expansion of offset press capacity is under study with the objective of bringing this profit centre to its full potential.

This division continues to receive a majority of its volume from Torstar companies and a commitment has been made to extend in-house printing as much as possible.

Film Production

Nielsen-Ferns Inc. has further diversified its film product with programming ranging from entertainment specials like "Karen Kain: Ballerina" to co-production of four episodes of "The New Avengers" series. Several new contracts for industrial-sponsored films and series were secured. The first two of seven one-hour episodes of "The Newcomers/Les Arrivants" were completed as part of a major historical drama series on the settling of Canada. This was commissioned as a 100th anniversary project by Imperial Oil.

Nielsen-Ferns is positioned to become a major supplier of programming to both the Canadian and international markets. Although no substantial contribution to earnings in the short term is anticipated, Nielsen-Ferns is a base from which to build Torstar's future participation in the entire broadcast/entertainment/leisure field.

Data Base Publishing

INFOMART, a joint operation with Southam Press Limited, is expanding its search and retrieval services. In addition to marketing access to more than 30 data bases of Systems Development Corporation, INFOMART recently signed an agreement to provide Canadian customers with access to the New York Times Information Bank. This current affairs data base covers some 70 worldwide publications. During the past year, INFOMART doubled its customer base.

Investments

In the third quarter Torstar Corporation increased its interest in shares of Western Broadcasting Company Limited of Vancouver to 32.9%. Western's extensive radio and television broadcasting operations in Canada continue to represent attractive potential for Torstar's investment in this complementary field.

Outlook

Acquisitions and investments over the past five years represent an outlay of $52 million. It is anticipated that combined investment capacity of the various companies in the Torstar group will be at least $150 million in the next five year period. Cash flow from newspaper and book publishing operations remains strong and it is expected that operating companies will be active in future acquisitions as well as in the further development of existing businesses.

Diversification has provided a sound base for the Corporation's continuing vitality. Like other newspaper publishers, Torstar recognized several years ago that a narrow profit base, highly susceptible to cyclical fluctuations in newspaper advertising, did not provide the stability required for solid growth. In 1972, some 74% of revenues were generated from advertising. In 1977, approximately 52% came from advertising. This reduced dependence on advertising has stabilized earnings. The profit base has been broadened by acquisition of book publishing and magazine operations; cash flow and credit resources have been utilized to support a faster rate of growth. That growth has been accomplished in a highly volatile economy and today the Corporation views the future in very positive terms.

People

Success in the Torstar group of companies is measured in terms other than growth in revenues and profit. Success is reflected in the excellence of our publications and their acceptance, daily, by millions of customers. It takes good people to achieve high standards and Torstar has developed a talented management and employee group to move the Corporation forward.

To all these Torstar people, the Directors offer their thanks and support.

Beland Honderich

Beland H. Honderich, Chairman
and Chief Executive Officer

Bill Dimma

William A. Dimma, President
and Chief Operating Officer

December 5, 1977

Summary of Financial Information

	1977	1976
Consolidated operating revenue	**$220,851,000**	$193,001,000
Net income		
— before extraordinary item	**$ 11,919,000**	$ 11,690,000
— after extraordinary item	**$ 12,181,000**	$ 12,711,000
Average shares outstanding	**8,086,650**	8,040,723
Earnings per share		
— before extraordinary item	**$1.47**	$1.45
— after extraordinary item	**$1.51**	$1.58
Dividends paid	**$ 2,588,000**	$ 2,332,000
Dividends per share	**32¢**	29¢

Consolidated Balance Sheet (thousands of dollars)

September 30, 1977 (with comparative figures at September 30, 1976)

Assets	**1977**	1976
Current:		
Cash	**$ 1,483**	$ 432
Short term investments, at cost, which approximates market	**19,061**	8,397
Receivables (note 2)	**26,043**	26,351
Inventories	**13,280**	8,982
Prepaid income taxes and other expenses	**7,400**	3,896
Total current assets	**67,267**	48,058
Investments and other non-current assets (note 3)	**31,385**	20,705
Fixed assets, at cost:		
Land	**3,311**	3,310
Buildings and leasehold interests	**5,884**	5,131
Presses and associated equipment	**16,894**	16,142
Non-press equipment and vehicles	**19,605**	17,712
	45,694	42,295
Less accumulated depreciation	**18,644**	15,631
Total fixed assets	**27,050**	26,664
Subscription list at amortized cost	**8,000**	8,333
Goodwill at amortized cost	**26,111**	23,955
Total assets	**$159,813**	$127,715

On behalf of the Board:

Director

Director

Torstar Corporation (incorporated under the laws of Ontario)

Liabilities and Shareholders' Equity	**1977**	1976
Current:		
Bank indebtedness	**$ 6,053**	$ 4,497
Accounts payable and accrued liabilities	**20,652**	16,276
Taxes payable	**14,673**	3,715
Dividends payable	**749**	643
Current portion of non-current debt	**3,558**	961
Total current liabilities	**45,685**	26,092
Non-current debt (note 4)	**21,445**	22,823
Deferred income taxes	**6,223**	6,249
Minority interest in subsidiaries	**11,174**	6,798
Employees' shares subscribed (note 5)	**724**	1,289
Shareholders' equity:		
Share capital (note 5) Issued and outstanding: 1977 – 8,087,353 shares (1976 – 8,043,153)	**12,452**	11,947
Retained earnings	**62,110**	52,517
Total shareholders' equity	**74,562**	64,464
Total liabilities and shareholders' equity	**$159,813**	$127,715

(See accompanying notes)

Auditors' Report

To the Shareholders of
Torstar Corporation:

We have examined the consolidated balance sheet of Torstar Corporation as at September 30, 1977 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements present fairly the financial position of the company as at September 30, 1977 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Clarkson, Gordon & Co.

Chartered Accountants
November 14, 1977
Toronto, Canada

Torstar Corporation Consolidated Statement of Income (thousands of dollars)

Year ended September 30, 1977 (with comparative figures for 1976)

	1977	1976
Revenue:		
Newspapers	**$133,727**	$130,195
Books and learning materials	**70,647**	47,811
Printing, magazines and film production	**24,506**	22,468
	228,880	200,474
Less intercompany printing revenue	**8,029**	7,473
Consolidated operating revenue	**220,851**	193,001
Consolidated operating costs (note 7)	**188,343**	164,566
Consolidated operating profit	**32,508**	28,435
Add (deduct):		
Investment revenue	**2,843**	2,367
Interest expense—non-current debt	**(2,408)**	(2,555)
—other	**(327)**	(411)
Net investment income (expense)	**108**	(599)
Amortization of goodwill (note 1)	**(702)**	(826)
Exchange adjustment	**158**	(438)
	(436)	(1,863)
Income before taxes	**32,072**	26,572
Income taxes	**15,384**	12,773
Income before minority interest and extraordinary item	**16,688**	13,799
Minority interest in earnings of subsidiary	**4,769**	2,109
Income before extraordinary item	**11,919**	11,690
Extraordinary item—income tax reductions arising from recovery of prior years' losses of subsidiaries	**262**	1,021
Net income for the year	**$ 12,181**	$ 12,711
Earnings per share:		
— before extraordinary item	**$1.47**	$1.45
— after extraordinary item	**$1.51**	$1.58

(See accompanying notes)

Torstar Corporation Consolidated Statement of Retained Earnings (thousands of dollars)

Year ended September 30, 1977 (with comparative figures for 1976)

	1977	1976
Retained earnings, beginning of year	**$ 52,517**	$ 42,138
Add net income for the year	**12,181**	12,711
	64,698	54,849
Less dividends (note 6)	**2,588**	2,332
Retained earnings, end of year	**$ 62,110**	$52,517

(See accompanying notes)

Torstar Corporation Consolidated Statement of Changes in Financial Position (thousands of dollars)

Year ended September 30, 1977 (with comparative figures for 1976)

	1977	1976
Source of funds:		
From operations –		
Income before minority interest and extraordinary item	**$16,688**	$13,799
Add charges to income which did not reduce working capital:		
Depreciation	**3,572**	3,045
Amortization of goodwill and subscription lists	**1,035**	1,160
Deferred income taxes	**(26)**	501
Total funds from operations	**21,269**	18,505
Increase in debt	**1,221**	24,500
Decrease in working capital	**384**	
Shares issued on acquisition of subsidiary		7,758
Extraordinary income tax reductions	**262**	1,021
Total source of funds	**$23,136**	$51,784
Application of funds:		
Investments in subsidiary and joint venture companies net of working capital acquired	**$ 4,424**	$20,367
Less portion of purchase price represented by a non-current liability	**(950)**	
	3,474	20,367
Investment in shares of Western Broadcasting Company Limited	**9,005**	4,422
Debt reduction	**3,549**	6,116
Fixed assets	**3,708**	2,736
Dividends to shareholders	**2,588**	2,332
Dividends paid by subsidiary to minority interest	**648**	601
Other	**164**	(244)
Increase in working capital		15,454
Total application of funds	**$23,136**	$51,784

(See accompanying notes)

Torstar Corporation Notes to Consolidated Financial Statements

September 30, 1977

1. Accounting policies

The following is a summary of significant accounting policies followed in the preparation of the consolidated financial statements:

(a) Principles of consolidation —
The consolidated financial statements include the accounts of all subsidiary companies.

(b) Foreign exchange —
The financial statements of foreign subsidiaries have been translated to Canadian dollars as follows: current assets and liabilities at exchange rates prevailing at September 30; fixed assets at exchange rates prevailing at dates of acquisition; income and expenses at average rates during the year. Exchange adjustments resulting from such translation practices are recognized in the consolidated statement of income.

(c) Inventories —
Inventories, other than newsprint, are valued at the lower of cost and net realizable value. Newsprint is valued at cost.

(d) Depreciation policy —
The cost of plant and equipment is depreciated using various rates and methods depending on the estimated useful lives of the assets. The rates and methods used for major depreciable assets are as follows:

(i) Presses and associated equipment — straight line over 15 years.

(ii) Non-press equipment — straight line over 12½ years or 20% diminishing balance.

(e) Subscription list —
The subscription list is amortized on a straight line basis over a 30-year period to 2001.

(f) Goodwill —
Goodwill which arose from acquisition of subsidiaries prior to April 1, 1974 was charged to consolidated retained earnings as at the dates of acquisitions. Goodwill which arises after that date is amortized over its estimated useful life on a straight line basis.

Goodwill carried on the consolidated balance sheet arose from Torstar Corporation's 1976 acquisition of Harlequin Enterprises Limited, and from acquisitions made by Harlequin and Torstar in 1977. An amortization period of 40 years is presently being used by all companies in the group. In the case of Torstar this represents a modification from the 30-year period used in 1976. This modification resulted in reducing 1977 amortization charges, and increasing net income, by $212,000.

(g) Past service pension costs —
The costs relating to improved pension benefits granted for employment in prior periods are amortized over the period of required funding, which is 15 years from the dates at which such benefits become effective.

(h) Income taxes —
The company follows the deferral method of income tax allocation which results in prepaid and deferred income taxes. Prepaid income taxes result from costs, principally provision for book returns, which are not currently deductible for tax purposes. Deferred income taxes result from claiming deductions for income tax purposes, principally depreciation, in excess of amounts currently charged.

2. Receivables

The provision for anticipated book returns deducted from receivables at September 30, 1977 amounted to $7,908,000 (1976 — $4,098,000).

3. Investments and other non-current assets

As at September 30, investments consisted of (in thousands of dollars):

	1977	1976
First mortgage sinking fund bonds due December 31, 2000 (a)	**$10,988**	$11,128
Second mortgage receivable maturing July 25, 2001 (a)	**4,409**	4,474
Shares of Western Broadcasting Limited, at cost (b)	**13,427**	4,422
Other non-current assets	**2,561**	681
	$31,385	$20,705

(a) The first mortgage sinking fund bonds are held on The Star building at One Yonge Street, and represent approximately one-half the total of such bonds outstanding. The second mortgage is also held on the One Yonge Street building.

(b) The investment in Western Broadcasting Company Limited is represented by 1,223,520 shares or approximately 33% of Western's outstanding common shares.

4. Non-current debt

As at September 30, non-current debt consisted of (in thousands of dollars):

	1977	1976
Bank loans due 1979-83 with interest at prime +1%	**$19,000**	$20,000
5½% first mortgage sinking fund bonds due 1978 (current liability in 1977)		2,493
Other debt due 1979-87 with interest at 6%-10%	**2,445**	330
	$21,445	$22,823

Non-current debt repayment requirements amount to $1,112,000 in fiscal 1979, $5,112,000 in 1980, $5,369,000 in 1981, $6,325,000 in 1982, $3,105,000 in 1983 and $422,000 in 1984 to 1987.

5. Share capital

(a) Authorized, issued and outstanding shares —
At September 30, 1977, shares authorized, issued and outstanding, all without par value, were as follows:

	Authorized	Issued and outstanding
Common	1,890,560	
Class B, Class C	10,828,477	6,315,830
Class D, Class E	3,571,523	1,771,523
	14,400,000	8,087,353

(b) Conversion and voting rights —
The Class B, C, D and E shares are interconvertible except that neither the Class B nor Class C shares (which only acquire voting rights upon failure of the company to pay quarterly dividends on Class B or Class C shares for eight consecutive quarters), are convertible into Class D or Class E shares (which have full voting rights under all circumstances).

(c) Restrictions on transfer —
The registration of a transfer of shares may be refused if such transfer could jeopardize either the ability of the company to engage in broadcasting or its status as a Canadian newspaper.

(d) Dividend entitlements —
After payment to the holders of Class C, D and E shares of dividends equal to the non-cumulative preferential dividend (7.5¢ per share) paid to the holders of Class B shares in any year, all shareholders of the company rank equally respecting the payment of any further dividends. Dividends on Class C and D shares may be paid in the form of tax-deferred dividends; in this event, the conditions attaching to the Class C and D shares provide that a suitable adjustment be made for taxes, if any, payable by the company with respect to such dividends.

(e) Employees' share purchase plan —
Under the company's employees' share purchase plan, employees may subscribe for Class B shares to be paid for through payroll deductions over two-year periods.

During the year 44,200 Class B shares were issued under the plan for a total cash consideration of $505,000. In October, 1977, a further 57,160 Class B shares were issued for a total cash consideration of $715,437. No further subscriptions are outstanding. Subscriptions under the plan have been temporarily suspended in order to comply with employee compensation legislation under the Canadian government's anti-inflation program.

6. Dividends

During the year the company declared dividends of 32¢ per Class B and Class E share and 85% of this amount per Class C and Class D share. With respect to dividends on the Class C and Class D shares, the company paid a tax of 15% on one quarterly dividend of 8¢ and has held back 15% on subsequent dividends pending passage of legislation which is expected to allow payment of such funds to Class C and Class D shareholders. The amount recorded as dividends in the consolidated statement of retained earnings includes the dividends paid plus the related tax and funds held back as described.

7. Consolidated operating costs

Operating costs for the year ended September 30 consisted of (in thousands of dollars):

	1977	1976
Newspapers —		
Employee costs	**$ 50,195**	$ 47,400
Paper and ink	**32,170**	30,095
Other	**40,011**	34,492
Total newspapers	**122,376**	111,987
Books and learning materials	**51,444**	39,238
Printing, magazines and film production	**22,552**	20,814
	196,372	172,039
Less intercompany printing purchases	**8,029**	7,473
Consolidated operating costs	**$188,343**	$164,566

8. 1977 acquisitions

During the year the company acquired an 80% interest in the shares of Nielsen-Ferns, Inc., a Canadian film production company, and acquired an additional 0.2% share of Harlequin Enterprises Limited, bringing its holdings to 52.6% of the shares of that company. In addition, Harlequin Enterprises Limited acquired a 100% interest in Ideals Publishing Corporation, a U.S. book publisher; and a 50% interest in Cora Verlag KG, a joint venture in Germany which markets romantic novels.

These acquisitions were accounted for as follows (in thousands of dollars):

Working capital	$ 100
Fixed assets	250
Other non-current assets	1,535
Net tangible assets, at fair value	1,885
Less minority interest in net tangible assets	219
	1,666
Goodwill	2,858
Total cost	$4,524

9. Options on shares of Harlequin Enterprises Limited

In connection with the 1976 acquisition of approximately 52% of the outstanding shares of Harlequin Enterprises Limited, the company entered into agreements with certain senior officers of Harlequin pursuant to which the company will have the option to buy from such officers, and the officers will have the option to sell to the company, 714,783 common shares of Harlequin. The agreements provide that such options may be exercised by either party during the periods from March 31 to June 30 in the years 1978 to 1981 as follows:

	Number of Shares
1978	125,087
1979	160,826
1980	196,565
1981	232,305
	714,783

The exercise of these options can be accelerated upon the occurrence of certain events. If, and to the extent that, the options are exercised, the purchase prices as provided for in these agreements will be the greater of:

(a) $8.83 per common share, and

(b) 10 times the fully diluted earnings per Harlequin common share before extraordinary items if such earnings are equal to or less than $1.50 per share, or $12\frac{1}{2}$ times the fully diluted earnings per Harlequin common share before extraordinary items if such earnings exceed $1.50 per share.

The earnings referred to above are defined as the earnings reflected in the consolidated income statement of Harlequin Enterprises Limited for the year ended December 31 immediately preceding the option period.

10. Pension plans

The unamortized past service costs for pension benefits in effect at September 30, 1977 approximate $4,300,000.

11. Lease obligations

The company has entered into a lease to 2001 for a portion of The Star building at One Yonge Street for an annual rental cost of $1.7 million plus municipal taxes, maintenance and other operating costs relating to the leased portion.

As part of the security given by the builder-owner to finance construction of The Star building, Torstar Corporation could be liable under certain contingencies to lease the whole building to 2001 with an additional rental commitment of approximately $1.1 million plus payment of related municipal taxes, maintenance and other operating costs.

Other long-term lease obligations are not considered material.

12. Other contingencies

(a) In 1975, the company commenced, and is proceeding with, an action for damages incurred for the failure of six printing presses provided by Crabtree-Vickers (Canada) to perform in accordance with the specifications pursuant to which they were sold.

(b) A number of legal actions against the company and its subsidiaries are outstanding, the ultimate disposition of which is not expected to materially affect the consolidated financial position of the company.

13. Statutory information

The aggregate remuneration charged to consolidated income in 1977 in respect of directors and senior officers (as defined by The Ontario Business Corporations Act) was $1,002,000.

14. Anti-inflation program

Under the Canadian government's anti-inflation program Torstar Corporation and its Canadian subsidiaries are subject to mandatory compliance with legislation which controls prices, profit margins, employee compensation and dividends to shareholders.

Operating revenue (thousands of dollars)	1972	1973	1974	1975	1976	**1977**
Newspapers	$77,911	$91,257	$104,388	$116,267	$130,195	**$133,727**
Books and learning materials	—	—	—	—	47,811	**70,647**
Printing, magazines and film production	4,420	8,263	16,158	19,090	22,468	**24,506**
	82,331	99,520	120,546	135,357	200,474	**228,880**
Less intercompany printing revenue	2,907	4,739	5,790	6,051	7,473	**8,029**
Consolidated operating revenue	$79,424	$94,781	$114,756	$129,306	$193,001	**$220,851**

Operating profit and net income (thousands of dollars)						
Newspapers	$10,224	$13,927	$ 16,873	$ 16,969	$ 18,208	**$ 11,351**
Books and learning materials	—	—	—	—	8,573	**19,203**
Printing, magazines and film production	342	438	408	945	1,654	**1,954**
Consolidated operating profit	10,566	14,365	17,281	17,914	28,435	**32,508**
Add (deduct):						
Net investment income (expense)	(1,265)	(367)	(546)	248	(599)	**108**
Amortization of goodwill	—	—	—	—	(826)	**(702)**
Exchange adjustment	—	—	—	—	(438)	**158**
Income before taxes	9,301	13,998	16,735	18,162	26,572	**32,072**
Income taxes	4,655	6,881	8,324	8,773	12,773	**15,384**
Income before minority interest	4,646	7,117	8,411	9,389	13,799	**16,688**
Minority interest in earnings of subsidiaries	—	—	—	—	2,109	**4,769**
Net income*	$ 4,646	$ 7,117	$ 8,411	$ 9,389	$ 11,690	**$ 11,919**

*excluding extraordinary items

Per share data (adjusted for stock splits)						
Net income*	64¢	97¢	$1.13	$1.26	$1.45	**$1.47**
Dividends	10¢	15¢	20¢	26¢	29¢	**32¢**
Shareholders' equity	$3.98	$4.80	$5.15	$6.18	$8.02	**$9.22**

*excluding extraordinary items

Rate of return on revenue						
Consolidated operating profit	13.3%	15.2%	15.1%	13.9%	14.7%	**14.7%**
Income before minority interest and extraordinary items	5.8%	7.5%	7.3%	7.3%	7.1%	**7.6%**

Torstar Corporation is a diversified communications company with primary interests in newspaper and book publishing. Toronto Star Newspapers Limited publishes Canada's largest newspaper. Harlequin Enterprises Limited is the world's largest publisher of romantic fiction. Other Torstar activities include magazine and community newspaper publishing, commercial printing, electronic data services and film production.

TORSTAR

Interim Report for the
second quarter ended
March 31, 1977

TO THE SHAREHOLDERS:

Consolidated operating revenue of Torstar Corporation totalled $105.9 million in the first six months of the 1977 fiscal year, compared with $92.9 million for the same period last year. Net income for the period amounted to $4,639,000 or 57c per share, a decline from $5,288,000 or 66c per share in the previous year.

For the second quarter alone, net income was $1,901,000 or 23c per share, up from $1,585,000 or 20c per share in the second quarter of fiscal 1976.

Earnings from The Toronto Star, down significantly in the first quarter, recovered to 1976 levels in the second quarter. The improvement results from tight cost controls in the face of continued softness in advertising volume, as well as from increases in National and Retail advertising rates introduced in January and February respectively.

Circulation of The Star in the six months ended March 31 (subject to audit) averaged 495,539 on Monday to Friday and 785,722 on Saturday. These averages are both higher than were achieved in the same period last year.

Negotiations to renew collective agreements with the Toronto Star's craft unions are in a post-conciliation stage. It is expected that these discussions will reach mediation later this month.

Harlequin Enterprises Limited, owned 52.7% by Torstar, maintained its strong earnings growth trend, with its contribution accounting for the gain in Torstar's consolidated income in the quarter ended March 31st. The volume of books sold in Harlequin's world-wide markets continued to increase, and price changes introduced in certain areas appear to be well received. Higher interest revenue in Harlequin, and a favourable exchange adjustment related to recent recovery of the British pound, were factors in the improved results.

The consolidated results for the second quarter are encouraging. Subject to economic conditions and the related demand for newspaper advertising, we are hopeful that this trend will continue for the rest of the year.

Beland Honderich W. A. Dimma

BELAND HONDERICH
Chairman and Chief
Executive Officer

WILLIAM DIMMA
President and Chief
Operating Officer

Toronto, Canada, May 4, 1977

CONSOLIDATED STATEMENT OF INCOME *(unaudited)*
(Thousands of dollars)

	Three Months Ended March 31		Six Months Ended March 31	
	1977	*1976*	*1977*	*1976*
Revenue:				
Newspapers	$32,121	$30,327	$66,445	$63,498
Books and learning materials	16,412	11,937	31,272	22,216
Printing, magazines and film production	5,722	5,269	12,357	10,605
	54,255	47,533	110,074	96,319
Less inter-company printing revenue	1,948	1,529	4,157	3,410
Consolidated operating revenue	52,307	46,004	105,917	92,909
Consolidated operating costs	46,726	41,018	92,706	78,973
Consolidated operating profit	5,581	4,986	13,211	13,936
Financial expense	697	665	1,443	1,430
Less investment revenue	761	534	1,273	998
Net financial expense (revenue)	(64)	131	170	432
Amortization of goodwill	222	206	472	411
Exchange adjustment	(72)	143	(155)	235
	86	480	487	1,078
Income before taxes	5,495	4,506	12,724	12,858
Income taxes	2,862	2,517	6,386	6,622
Net income before minority interest	2,633	1,989	6,338	6,236
Minority interest in earnings of subsidiaries	732	404	1,699	948
Net income	$1,901	$1,585	$4,639	$5,288
Per share: Net income	23c	20c	57c	66c
Dividends	8c	7c	16c	14c

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION *(unaudited)*
(Thousands of dollars)

	Six Months Ended March 31	
	1977	*1976*
Source of funds:		
From operations —		
Net income	$ 4,639	$ 5,288
Add charges (credits) to income which did not reduce working capital:		
Depreciation and amortization	2,247	2,014
Deferred income taxes	177	(57)
Minority interest in earnings of subsidiaries	1,699	948
Total funds from operations	8,762	8,193
Increase in long term debt	3,473	22,500
Shares issued on acquisition of subsidiary	—	7,758
Total source of funds	$12,235	$38,451
Application of funds:		
Acquisition of subsidiaries (including working capital of $224,000 in 1977 and $10,260,000 in 1976)	$ 3,033	$30,627
Dividends to shareholders	1,294	1,125
Increase in working capital	3,647	2,064
Additions to fixed assets	1,761	1,688
Increase in investments	2,148	—
Debt reduction	—	2,802
Dividends paid by subsidiary to minority interest	324	307
All other (net)	28	(162)
Total application of funds	$12,235	$38,451